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UNCLAS SECTION 01 OF 05 BANGKOK 005699

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DEPT FOR EAP/MLS AND EB
TREASURY FOR OASIA
COMMERCE FOR 4430/EAP/MAC/OKSA
STATE PASS TO USTR FOR WEISEL, COEN

E.O. 12958: N/A
TAGS: ECON EFIN FAID TH
SUBJECT: THAILAND: CAPITAL ALLOCATION TO TSUNAMI VICTIMS

REF: A. BANGKOK 0155

1B. BANGKOK 0950

Introduction and Summary

11. The streets of Patong Beach are busy, not as busy as normal and with a distinct scarcity of the Asian tourists typical during the summer months that comprise the low tourist season in Phuket, but still enough to give the place a certain buzz. Hotels report a 40-50 percent occupancy rate, about 10-15 percent below normal for this time of year and a marked recovery from the 10-20 percent rates that prevailed during the first half of the year. Some of the large hotels are not yet fully operational, using the tsunami recovery period and damage they incurred as reasons to remodel. Street vendors still crowd the sidewalk along Beach Road and the bars and nightclubs are all open, albeit at some the bar girls outnumber the clientele. (After the tsunami, many bar girls simply went to work in other Thai tourist centers. Their return is a positive sign; an indication that they again see sufficient business potential to return from Bangkok or Pattaya). We observed very few empty storefronts although business was slow.

People involved in real estate advised that property prices have continued to appreciate, not declining even immediately after the disaster. The Phuket branch of a Thai bank reported that the volume of transactions at its currency exchange facilities was down only 14 percent from the same period last year. As several businessmen told us, over the past 4 years they have survived the effects of the Bali bombing, SARS, avian flu and now the tsunami. They are hopeful that their run of bad luck will end and they can soon end the discounting being used to lure back bargain-hunting tourists.

12. In contrast, tsunami economic recovery in the province of Phang Nga has barely begun. Only about 20 percent of the province's pre-disaster hotel rooms (1200 of 6000) are now habitable, and yet there is only 10 percent occupancy. In the Khaolak area, which was the center of the province's tourist industry, unemployment is reportedly around 70 percent. While the selling price for fish is good, the number of fisherman and large commercial shipping vessels is about half of what it was. The shrimp hatchery and shrimp farm businesses in the province were largely wiped out and have made little progress towards reconstruction. If not for the rubber, cashew and papaya plantations -which are currently enjoying high prices- combined with the inflow of funds from the international NGOs that have blanketed the affected areas, the Phang Nga economy would be a complete ruin.

13. The RTG has used commercial banks and government-owned specialized banking institutions to channel credit to tsunami-affected businesses. While this has been effective in

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restructuring existing loans, relatively little in the way of new money needed for reconstruction has been extended. In addition, those without previous bank relationships or who have insufficient collateral have a very difficult time acquiring credit beyond the maximum US\$12,500 offered by the government's Small and Medium Enterprise Bank to those who can find a credit-worthy co-signer. The often informal nature of many SMEs in Thailand, a reluctance of many entrepreneurs to engage with the government, and a failure of businesses or their communities to organize to have themselves heard and demand assistance has hindered their ability to take full advantage of those assistance programs that are available. NGOs have stepped into the breach to satisfy humanitarian needs but have also created some degree of dependency and, by offering some goods and services for free, have hindered the re-start of some sustainable businesses. End Summary and Introduction.

Government Assistance

14. The Thai government says it has spent about US\$650 million on tsunami support and reconstruction. How much of this has been spent vs. how much has been allocated is not clear. In Phuket, US\$1.78 million has been distributed to 1200

individuals as compensation for the destruction or damage to their homes. Each family that has lost a family member is entitled to a Bt20, 000 (US\$486) lump-sum payment which would total Bt62.9 million (US\$15.3 million) for the 3147 Thai citizens who have been confirmed dead (2817 people remain missing and 1650 bodies have yet to be formally identified). The RTG through the Royal Thai Army has reportedly built 1456 homes at a cost of Bt100, 000 (US\$2400) each for a total housing spend of about US\$3.5 million. Other funds have reportedly been spent by the Fishery Department (US\$15 million on fishing boats in Phuket only, no figures for Phang Nga). The new houses are not always of the quality or style appropriate to the situation: southern Thai families typically live three generations to a house, five to ten persons, but the RTG provides only a single house of 36 square meters (387 sq feet). Also, many fishermen own land on tidal flats and, appropriately, built their homes on stilts. The RTG-supplied homes are built on cement slabs on the ground. Land title disputes have slowed the provision of new houses to hundreds of families and there are accusations of land-grabbing by powerful figures including the sister of the Speaker of Parliament. Schools and hospitals have been rebuilt but much of the money and labor for these (as for other houses not included above) have been provided by NGOs. Critics of the government claim that the amount the RTG says it has spent and the observed results don't match and assume that there must be fraud. Others argue that the number of RTG agencies, NGOs, foreign governments and individuals that have flowed into the region have resulted in significant problems in coordination and resulting waste. Some school rebuilding projects, for example, have more resources than needed, others not enough.

Capital Allocation and Commercial Banks

15. As a means to funnel capital to businesses affected by the tsunami, the Bank of Thailand (BoT, the central bank)

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instituted a "soft loan" program. The BoT made available Bt60 billion (US\$1.45 billion) for loans to commercial banks and specialized government lending institutions (Government Savings Bank-GSB, Bank for Agriculture and Agricultural Cooperatives-BAAC, and the Small and Medium Enterprise Bank). The program provides loans to banks at a rate of 0.01 percent for three years with the following provisions:

- The banks use the funds only for lending to those affected by the tsunami.
- The banks charge these customers no more than 2 percent per year.
- If a borrower had insurance coverage for their loss, they were ineligible.
- The borrower must be at least 50 percent Thai-owned.
- Banks had only until February 1, 2005 to apply, seeking approval from the BoT for each loan they wished to include under the program.
- The soft loans would apply only to 80 percent of the total loan amount. The banks must apply 20 percent of the loan amount from its own capital. Normal underwriting standards would apply.

16. BoT reported that it had approved loan requests for Bt48 billion, of which Bt37.5 billion was for hotels and restaurants, Bt1.3 billion for construction (mainly private roads and other infrastructure), Bt900 million for transportation (cruise boats, taxis), Bt400 million for fisheries and Bt180 million for agriculture. As of August 21, Bt25 billion (US\$607.8 million) had been drawdown, mostly for large hotels.

17. In fact, the vast majority of money from the BoT program has to date been used for refinancing existing loans to tsunami-affected companies. Old loans were turned into new

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three year loans, often with interest and/or principle grace periods of 6 months to 3 years. While this has provided some breathing room for borrowers, the banks have been extremely reluctant to extend new loans either to existing borrowers or new clients unless the borrower has collateral (cash, land and buildings only) sufficient to cover the entire amount of both the existing loan and the new loan. There are a variety of explanations for the reluctance of the banks to extend new money in addition to the lack of available collateral. These include:

- Time required to renegotiate old loans and a new loan (two separate negotiations)
- Borrowers waiting to decide on whether/when to rebuild based on recovery outlook.
- Lack of clear title to land.
- Banks waiting to see strength of recovery before extending new loans in the region.
- Banks waiting for insurance companies to complete their settlements with borrowers before extending new loans.
- Bank's reluctance to extend loans based on 2 percent

margins (typical bank margins on commercial loans are at least 4 percent.)

-Concern over reports of high levels of fraud, people claiming the loss of their fishing boat several times over, for example. As a result, there is some hesitancy among the banks to respond to some types of loan requests.

The BoT is satisfied with these results given that the stability of the banking system is the central bank's primary concern. The conservative approach the commercial banks have taken utilizing the soft-loan is seen as contributing to tsunami recovery while apparently not increasing banking

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system exposure to high-risk borrowers.

The Special Purpose Banks

18. Small and micro businesses (e.g. sidewalk vendors, taxis, small restaurants, fisherman with a 12 foot boat, small-scale merchants) typically don't have formal bank relationships. Commercial banks view this business as high-risk and low profit. The RTG has directed the GSB, BAAC and SME Bank to service this sector and develop special programs to aid tsunami victims.

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19. The GSB has three types of loan programs for tsunami victims:

- Support loans for small businesses of a maximum Bt100, 000 (US\$2400) with no collateral required but one guarantor/co-signer.

-Using the BoT soft-loan program. No maximum amount for the loan but the borrower must have sufficient collateral. This has been used for existing GSB clients.

-SME support loans. Loans up to Bt300, 000 (US\$7200) may be extended without collateral but require two guarantors/co-signers. Loans of more than Bt300, 000, up to a maximum of Bt5 million (US\$121,000) must be fully collateralized.

The GSB reports that they have extended Bt100 million (US\$2.4 million) to 900 existing customers and 100 new customers. We note that since GSB says they have refinanced all existing tsunami-affected customers, there was probably very little in

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the way of fresh credit extended under any of the bank's programs. We are told a key problem is the need for guarantors. A village leader told us that he could not act as a guarantor since that person must be a civil servant. Others told us that anyone could co-sign.

10. The SME Bank branches in Phuket and Phang Nga approved 433 loans post-tsunami, the vast majority for amounts ranging from Bt50,000 (US\$1250) to Bt500,000 (US\$12,500) to those affected by the waves directly (destruction or damage) or indirectly (loss of business). For loans of this size, no collateral is required but at least one guarantor. Most of the borrowers are new customers of the bank, typically retail or wholesale firms but also includes tour operators, restaurants and small manufacturers. Total amount of the loans extended to small clients (other than agriculture -related which is the purview of the BAAC) has been US\$4.5 million. Some larger new clients, mostly hotels, have also been taken on by the bank, in cases where the client's existing bank declined to make additional loans for reconstruction. The SME Bank requires full collateral to extend loans to these larger customers and for existing loans to be restructured under the BoT program. Every commercial bank and the other specialized banks pointed to the SME Bank as the only opportunity for those without sufficient collateral to get a small loan. The small number of loan applicants compared to the thousands of small businesses affected was noted by the branch managers.

11. The Department of SME Promotion has also created a "venture capital fund" to provide an alternative source of capital for companies with capitalization of between US\$25,000 and US\$5 million... Rather than take an equity position, the fund takes a promissory note back from the company carrying an interest rate of 1 percent yearly with a five-year maturity. The fund has a total capital of US\$125 million supplied by the SME Bank, the Stock Exchange of Thailand and its listed companies and the Thai Bankers Association. A private equity firm acts as the fund manager. It has invested US\$50 million in 14 medium-sized hotels in Phang Nga. In order for the fund to invest, existing loans must have been restructured under the BoT program and sufficient collateral to back the note must be available.

12. The BAAC lends only to farmers, fisherman and the food processing industry. BAAC officials told us that 6343 of their customers had damage to physical property and/or loss of income resulting from the tsunami with total outstanding debt of Bt622 million (US\$15.2 million). Of this, 112

customers died in the wave and their debt of Bt19.3 million (US\$472 thousand) was written-off. 5716 customers had their loans restructured to require no principle or interest payments for three years and no interest accruing during that period. The Ministry of Finance is defraying the cost of interest foregone by BAAC. The remaining 515 customers are reportedly "in process." The BoT soft-loan program is used for providing new loans to existing customers. To date, 2307 new loans totaling Bt194.5 million (US\$4.7 million) has been drawdown even though the BoT has provided Bt1 billion to BAAC in pre-approvals. The maximum size of this loan is Bt150, 000 (US\$2037) with no collateral required but two existing BAAAC customers to act as guarantors. No new customers have yet been provided loans, although the BAAC is considering making the BoT funds available to this group of customers as well.

Where are the Customers?

13. The apparent underutilization of the programs to provide credit to the tsunami victims and their businesses is ascribed to a variety of factors:

- The victims are too traumatized to understand what is available or lack the energy to travel to the district capitals (where these programs are typically administered) to request the loan.
- The programs are poorly publicized. Even when people are aware of their existence, there tend to be widespread rumors about who is or is not eligible and what is required to secure a loan.
- There is a high degree of effort required to comply with Thai company law. This includes filing monthly tax statements. Many small businesses prefer to simply operate on an unregistered basis. This, of course, means that they have no paper proof of their operations as having existed prior to the tsunami. While the specialized institutions say they will accept, in lieu of registration documents, the written assurance of a village leader affirming that prospective borrower had an operation before the disaster, we have heard of very few examples where this process worked.
- Some sectors are simply written-off by the banks. Shrimp hatcheries in particular are seen as un-creditworthy. Commercial fishing boats (costing US\$200,000 and up) are not considered a fixed asset (they move) and so are not eligible for loans without other, fixed, collateral.
- There is a culture of dependency forming in some villages. With foreign NGOs rebuilding homes and supplying food, medicine and often cash, "many people would prefer spending their day waiting in line for a handout rather than out fishing" as one Thai NGO official told us. This also reduces efforts to get loans.
- Many businesses in Phuket, while registered as majority Thai-owned, are in fact majority owned and operated by foreigners. Thai banks are apparently unwilling to extend their tsunami relief programs to foreigners regardless of the official ownership registration.
- The number of NGOs providing free food and free fishing boats has impaired the ability of commercial vendors of these products to compete. These small businesses see no reason to take on additional debt until the market reverts to normal.

14. The end result has been that in Phuket, one of the nation's richest provinces with a long-standing tourist industry and businesses that have had the opportunity to build cash reserves over many years of operation, the need for access to bank capital is less critical than in Phang Nga where the tourist industry only really began in the late 1990s, many businesses were relatively smaller and the damage was considerably more extensive. Commercial banks have largely declined to make loans to entities that were not customers before the tsunami; some banks will not consider any new customers at all, preferring to await the results of the tourist high-season before even considering the possibility. The specialized banks have focused on small loans. We believe that one reason there are so many more BoT loan approvals than drawdowns is that the banks are not making decisions on pending requests for new loans from customers until after this tourism season. Even then, sufficient collateral will be a requirement, not an easy prerequisite since many businesses, especially in Phang Nga, had borrowed close to the full value of the collateral and land prices in that province are said by some observers to have declined considerably in the wake of the slow post-tsunami recovery.

Comment

15. The provision of assistance and credit to tsunami-affected individuals and businesses has been uneven.

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This is attributable to such universal factors as bureaucratic error, coordination difficulties and oversight in difficult circumstances and to cultural issues related to

hesitancy among some poor Thais to deal with the government or other large organization that they find overwhelming. The RTG effort to use existing credit institutions, both public and private, to allocate capital and credit in the tsunami region can be seen as a noble free market experiment under which the government provided incentives for these institutions to provide debt relief and new capital while maintaining disciplined lending standards. Unfortunately, Thai banks have never lent against cash-flow. Collateral and "personal relationships" have always been the credit criteria when evaluating credit risk. The downside of this approach is clear in the aftermath of the tsunami. The strict reliance on land and buildings as collateral for the full value of any loan of more than a few thousand dollars has prevented businesses, especially in Phang Nga, from acquiring the means of restarting their business. Further, with the decline in business, the value of real estate collateral tends to decline and the situation further deteriorates.

¶16. At some point, private equity will step in and purchase the distressed assets. Meanwhile, the banks have used the BoT soft-loan program to delay the day of reckoning for their customers for three years. (When the BoT program ends). It is clear that both the BoT and the banks have used this program primarily as a way to avoid booking any loans as non-performing rather than a real restructuring that examines the viability of the loan going forward. If the borrowers are able to find a way to get back on their feet during the three-year loan term, all will be well; if not, then the banks will deal with the issue at that time. In the interim there is considerable frustration and a sense among small businesses and individuals that, once again, the big and powerful get what they need and the small get little. With the RTG's pronouncements that it needed no foreign assistance, that it has spent large amounts on reconstruction already and questions about where the funds raised for tsunami relief (by the "Prime Min

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ister's Fund" for example) have gone, one might think the frustration level could reach a point of ignition. But Phuket is coming back in any case, and Phang Nga is simply too poor and its society too poorly organized to result in any sort of real backlash, especially with the international NGOs on hand to provide for people's needs. On September 6, the RTG cabinet will hold a meeting in Phang Nga in response to the slow recovery of that province.

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